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IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1957.

T. V. WILLIAMS as State Revenue Commissioner,
Petitioner,

vs.

STOCKHAM VALVES AND FITTINGS, INC.,
Respondent.

On Writ of Certiorari to the Supreme Court of Georgia.

BRIEF FOR THE PETITIONER.

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No. 763.

IN THE

SUPREME COURT OF THE UNITED STATES.

OCTOBER TERM, 1957.

T. V. WILLIAMS as State Revenue Commissioner,
Petitioner,

vs.

STOCKHAM VALVES AND FITTINGS, INC.,
Respondent.

On Writ of Certiorari to the Supreme Court of Georgia.

BRIEF FOR THE PETITIONER.

OPINION BELOW.

The opinion and judgment of the Supreme Court of Georgia (R. 28-38) is reported in 213 Ga. 713, 101 S. E. 2d 197.

JURISDICTION.

The judgment of the Supreme Court of Georgia was entered on November 8, 1957, and a rehearing was denied on November 26, 1957. The petition for a writ of certiorari was filed in this Court on February 3, 1958, and the order granting certiorari was entered on March 17, 1958. The jurisdiction of this Court is invoked under 28 U. S. C. 1257 (3) since the validity of state statutes on grounds of repugnancy to the Constitution of the United States is drawn in question.

QUESTIONS PRESENTED.

The questions presented are whether the Georgia statutes which impose a general tax, without discrimination, directly upon net income (not a franchise, occupation, privilege or license tax measured by net income), fairly apportioned according to a taxpayer's activities within Georgia, violate either the commerce clause (Article I, Section 8, Clause 3) or the due process clause (Fourteenth Amendment) of the Constitution of the United States, as applied to a foreign corporation which maintained permanently within Georgia a sales service office and sales service employees and which engaged regularly and competitively within Georgia in a variety of sales service activities when all of its sales were consummated at its home office outside Georgia and all of its activities within Georgia were in connection with such sales?

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED.

Section 8, Clause 3 of Article I of the Constitution of the United States provides:

> "The Congress shall have power . . . to regulate commerce . . . among the several states. . . ."

Section 1 of Amendment XIV of the Constitution of the United States provides:

> ". . . nor shall any State deprive any person of life, liberty, or property, without due process of law; . . ."

Section 92-3102 of the Code of Georgia of 1933[1] provides:

> "Rate of taxation of corporations—Every domestic corporation and every foreign corporation shall pay annually an income tax equivalent to five and one-half per cent. of the net income from property owned or from business done in Georgia, as defined in Section 92-3113."

Section 92-3113 of the Code of Georgia of 1933[2] provides:

> "The tax imposed by this law shall apply to the entire net income, as herein defined, received by every

---

[1] Codifying Section 4 of the Income Tax Act of 1931 (Ga. Laws 1931, Ex. Sess., 24, 26) as amended and in effect for the taxable years 1952, 1954 and 1955, except that the rate was reduced to four percent for taxable years beginning on or after January 1, 1955.

[2] Codifying Section 15 of the Income Tax Act of 1931 (Ga. Laws 1931, Ex. Sess., 24, 26) as amended and in effect for the taxable years 1952, 1954 and 1955. Italicized portion was added by 1950 amendment (Ga. Laws 1950, 299, 300-303). For full text including further provisions for allocating and apportioning net income from business done partly within and partly without the State, see Appendix, infra, 57.

corporation, foreign or domestic, owning property or doing business in this State. **Every such corporation shall be deemed to be doing business within this State if it engages within this State in any activities or transactions for the purpose of financial profit or gain, whether or not such corporation qualifies to do business in this State, and whether or not it maintains an office or place of doing business within this State, and whether or not any such activity or transaction is connected with interstate or foreign commerce. . . .**"

STATEMENT OF THE CASE.

For the taxable years 1952, 1954 and 1955 Petitioner, as State Revenue Commissioner of the State of Georgia, assessed and collected as Georgia income taxes, pursuant to the aforesaid Sections 92-3102 and 92-3113, $18.73, $489.48 and $970.10 respectively, from Respondent. In due time, Respondent filed claims for refund of the aforesaid taxes and these claims were denied by Petitioner (R. 2).

Thereafter, in due time, Respondent filed a suit against Petitioner to recover the aforesaid taxes. In its petition Respondent neither disputed the computation of these taxes nor the reasonableness of the apportionment of its net income to Georgia under the statutory apportionment formula prescribed by the further paragraphs of Section 92-3113; no discrimination was charged. It based its right to recover squarely upon the unconstitutionality of Sections 92-3102 and 92-3113 under the commerce clause (Article 1, Section 8, Clause 3) and the due process clause (Fourteenth Amendment) of the Constitution of the United States as applied to its activity within the State of Georgia, which it characterized as being entirely in interstate commerce and entirely beyond the territorial limits of the State of Georgia (R. 21-25). These were the only questions of law raised by Respondent's petition.

The case was tried on an agreed stipulation of facts which is in the record before the Court (R. 1-13). Briefly the important facts are:

During the tax years in question, Respondent was a Delaware corporation with its principal office and manufacturing plant at Birmingham, Alabama. It was engaged in the business of manufacturing and selling valves and pipe fittings and in promoting the sale of these products. Purchasers of its products were established local wholesalers and jobbers located in all of the United States. It maintained inventories of its products in established warehouses at Birmingham, Alabama, Philadelphia, Pennsylvania, Chicago, Illinois, Houston, Texas, and Vernon, California. It maintained established sales service offices at the above locations and also at Cambridge, Massachusetts, New York, New York, Pittsburgh, Pennsylvania, San Francisco, California, Washington, D. C., Dallas, Texas, St. Louis, Missouri, and **Atlanta, Georgia** (R. 2, 3).

Respondent accepted all orders at its Birmingham office and made all deliveries "f. o. b. warehouse" (R. 4, 5). In other respects it meticulously followed the customary procedures that foreign corporations have adopted for insulating themselves from local obligations (R. 8, 9).

But this is not all. The details of Respondent's method of operation, using these established sales service offices, and, particularly its sales service activities through its Atlanta office and Atlanta representative, in summary, show that Respondent's activity in and through its Atlanta office and its Atlanta representative was no casual, transitory, spasmodic, traveling-drummer type of activity—they show that Respondent permanently, designedly, and competitively engaged in soliciting business and in many additional activities and services within Georgia, the total purpose and effect of which was to establish, identify, and

operate its Atlanta office and its Atlanta representative as local in the same sense as its competitors who sold comparable products from local inventories in Georgia (R. 3-8).

The trial court found that Respondent, "during the tax years in question, engaged in substantial activities within the State of Georgia for financial profit or gain within the meaning of Code Section 92-3113 . . . that the taxes collected by Defendant from Plaintiff under Code Section 92-3102, being taxes on Plaintiff's net income fairly apportioned according to its activities within the State of Georgia, did not constitute a burden on interstate commerce nor were they levied or collected in violation of due process under the Federal Constitution as alleged by Plaintiff's petition" (R. 13, 14).

On appeal to the Supreme Court of Georgia this judgment was reversed (R. 28). Now this judgment is before this Court on writ of certiorari (R. 39).

SUMMARY OF ARGUMENT.

A. *The Interstate Commerce Aspect.*

1. A tax on net income is a tax on the realization of gain from property or economic activity; it is not a tax on the property or economic activity which is the source of the gain. This proposition, first applied by the Court to interstate income forty years ago in **United States Glue Co. v. Town of Oak Creek**, 247 U. S. 321, 38 S. Ct. 499, 62 L. Ed. 1135 (1918), along with **Peck & Co., Inc., v. Lowe**, 247 U. S. 165, 38 S. Ct. 432, 62 L. Ed. 1049 (1918), represented new thinking on the part of the Court; it has gathered strength over the years by reaffirmation in **Metcalf & Eddy v. Mitchell**, 269 U. S. 514, 46 S. Ct. 172, 70 L. Ed. 384 (1926) and **Graves v. New York ex rel. O'Keefe**, 306 U. S. 466, 59 S. Ct. 595, 83 L. Ed. 927 (1939); it was directly applied to a foreign corporation engaged exclusively in interstate commerce in **West Publishing Co. v. McColgan**, 328 U. S. 823, 66 S. Ct. 1378, 90 L. Ed. 1603 (1946), affirming per curiam the Supreme Court of California, 27 Cal. 2d 705, 166 P. 2d 861 (1946); it has emerged as bedrock in income taxation—both state and federal—and precludes any contention that a net income tax is a direct tax on interstate commerce.

2. A general tax on net income derived exclusively from interstate commerce is neither *per se* a franchise tax, nor *per se* a tax on gross receipts. A general tax on net income **as such** is itself a constitutional channel by which interstate commerce can be required to share in the tax burden of the states in which it operates. The effort by fair apportionment to establish the franchise tax as another constitutional channel for this purpose, aborted in **Spector Motor Service, Inc., v. O'Connor**, 340 U. S. 602, 71 S. Ct. 508, 95 L. Ed. 573 (1951), proceeded on the premise that a franchise tax measured by net income is like a net

income tax, not that a net income tax is like a franchise tax. The "tangled underbrush of past decisions" seeking to justify franchise taxes on the basis of "a local incident" have no relevance with respect to a general income tax. Nor is a general tax on net income *per se* a tax on gross receipts; it takes no toll from each interstate transaction. Reducing the base of a tax from gross receipts or gross income to net income does more than justify the tax by limiting it to profitable businesses; it indicates a concern with taxing gain as such and no concern with taxing the activity epitomized by gross receipts.

3. A general tax on net income, like a property tax, does not unduly burden interstate commerce. Neither the property of a private corporation used exclusively as an instrumentality of government, nor its income, enjoys any immunity from state taxation. **M'Culloch v. Maryland**, 4 Wheat. 316, 4 L. Ed. 579 (1819); **Railroad Company v. Peniston**, 18 Wall. 5, 21 L. Ed. 787 (1873); **Metcalf & Eddy v. Mitchell**, 269 U. S. 514, 46 S. Ct. 172, 70 L. Ed. 384 (1926). The property of a private corporation used exclusively in interstate commerce or as an instrumentality of interstate commerce likewise enjoys no immunity from state taxation. **Old Dominion Steamship Co. v. Virginia**, 198 U. S. 299, 25 S. Ct. 686, 49 L. Ed. 1059 (1905). Neither should its income.

B. *The Due Process Aspect.*

1. Due process does not prohibit the taxation of income of a non-resident earned within the taxing state. **Shaffer v. Carter**, 252 U. S. 37, 40 S. Ct. 221, 64 L. Ed. 445 (1920); **New York ex rel. Whitney v. Graves**, 299 U. S. 366, 57 S. Ct. 237, 81 L. Ed. 285 (1937).

2. Due process, for in personam jurisdictional purposes, requires only "minimum connections." The Court no

longer bases in personam jurisdiction over a foreign corporation circuitously on "presence," "doing business" or "consent," but directly on purposeful activities done on its behalf by its agents and employees within the state seeking jurisdiction. **International Shoe Co. v. Washington,** 326 U. S. 310, 66 S. Ct. 154, 90 L. Ed. 95 (1945); **McGee v. International Ins. Co.,** 355 U. S. 220, 78 S. Ct. 199, 2 L. Ed. 223 (1957). The test is "minimum connections." **Miller Bros. Co. v. Maryland,** 347 U. S. 340, 74 S. Ct. 535, 98 L. Ed. 744 (1954).

3. The continuous, designed and competitive exploitation of the markets of the taxing state constitutes sufficient connection to satisfy due process. Even though the activities of a foreign corporation are exclusively interstate commerce they are nonetheless physically within some state, and activities which meet the requirements of due process for purposes of service also meet the requirements of due process for purposes of taxation. It is the **quality** of the connections, their regularity, continuity and deliberate design, and not the quantity that is important. **International Shoe Co. v. Washington,** 326 U. S. 310, 66 S. Ct. 154, 90 L. Ed. 95 (1945); **General Trading Co. v. State Tax Commission,** 322 U. S. 335, 64 S. Ct. 1028, 88 L. Ed. 1309 (1944).

4. Due process also requires, for income taxing purposes, that the income have a situs or source within and limited to the taxing state. **Hans Rees' Sons v. North Carolina,** 283 U. S. 123, 51 S. Ct. 385, 75 L. Ed. 879 (1931). This is a second requirement of due process independent of "minimum connections". Income has a situs according to the property or activity which produces the income. **Shaffer v. Carter,** 252 U. S. 37, 40 S. Ct. 221, 64 L. Ed. 445 (1920).

5. A fair apportionment statute reflects income having a situs or source within the taxing state and necessarily

establishes that the taxing state has afforded the recipient thereof "opportunities, benefits or protection." **Underwood Typewriter Co. v. Chamberlain**, 254 U. S. 113, 41 S. Ct. 45, 65 L. Ed. 165 (1920); **Butler Bros. v. McColgan**, 315 U. S. 501, 65 S. Ct. 701, 86 L. Ed. 991 (1942); **Ott v. Mississippi Valley Barge Line Co.**, 336 U. S. 169, 69 S. Ct. 432, 93 L. Ed. 585 (1949); **Braniff Airways, Inc., v. Nebraska**, 347 U. S. 590, 74 S. Ct. 757, 98 L. Ed. 967 (1954).

C. *The Multiple Burdens Aspect.*

1. Given a general income tax on fairly apportioned net income, the threat of a second income tax on entire net income at the taxpayer's domicile merely raises the long-time question of whether due process prohibits more than a single situs for the taxation of income. In **Shaffer v. Carter**, 252 U. S. 37, 40 S. Ct. 221, 64 L. Ed. 445 (1920), the Court unequivocally authorized, under due process, a taxable situs for income at its source. In **Lawrence v. State Tax Commission**, 286 U. S. 276, 52 S. Ct. 556, 76 L. Ed. 1102 (1932), the Court, under due process, allowed income also to be taxed at the domicile of its recipient. While **Lawrence** created a threat of multiple taxation, it also decided that due process is not violated thereby.

2. However, if the commerce clause prohibits what the due process clause allows, that is, the foregoing threat of multiple taxation, the state of domicile or principal office is required to yield, not the state or states in which the income is earned. **Standard Oil Co. v. Peck**, 342 U. S. 382, 72 S. Ct. 309, 96 L. Ed. 427 (1952).

3. As among states from which income is derived, a fair apportionment formula by its nature precludes multiple taxation of the total net income. If conceivably more than 100%, as a practical matter, can be taxed, it is because

the taxpayer has failed to carry the burden of showing an unreasonable formula or because apportionment formulas used among the several income-taxing states are not uniform in their make-up.

4. The burden of keeping records and filing returns as required by the various states in which a taxpayer chooses to do business and in which it earns its income is no more than an incidental burden on interstate commerce and does not invalidate an otherwise constitutional channel of taxation.

ARGUMENT AND AUTHORITIES.

A. *The Interstate Commerce Aspect.*

We, of course, concede that the commerce clause by its own force creates an area of trade free from interference, including taxation, by states in which this trade takes place. **Freeman v. Hewit**, 329 U. S. 249, 67 S. Ct. 274, 91 L. Ed. 265 (1946). However, this freedom, as it relates to state taxation, is not absolute; there are constitutional channels by which a state can validly make interstate commerce pay a fair share of its tax burden. **Spector Motor Service, Inc., v. O'Connor**, 340 U. S. 602, 71 S. Ct. 508, 95 L. Ed. 573 (1951).

Now, for forty years, since 1918, the decision in **United States Glue Co. v. Town of Oak Creek**, 247 U. S. 321, 38 S. Ct. 499, 62 L. Ed. 1135 (1918), has stood for the proposition that a general net income tax on interstate income is a constitutional channel by which interstate commerce can be required to pay its way. Whatever question remained after **U. S. Glue**, stemming from the fact that the taxpayer was a domestic corporation and engaged also in local activity, was dispelled by the decision in **West Publishing Co. v. McColgan**, 328 U. S. 823, 66 S. Ct. 1378, 90 L. Ed. 1603 (1946), affirming per curiam the decision of the Supreme Court of California, 27 Cal. 2d 705, 166 P. 2d 861 (1946), where the taxpayer was a foreign corporation engaged in exclusively interstate activity.

The present challenge of this long-established proposition is apparently prompted by the 1951 decision in **Spector Motor Service, Inc., v. O'Connor**, 340 U. S. 602, 71 S. Ct. 508, 95 L. Ed. 573. More particularly, it can be traced to footnote 6 of the majority opinion in that case which is

interpreted by some to treat a franchise tax[3] measured by net income and a general tax on net income as the same thing and to imply that the validity of a general net income tax applied to exclusively interstate income is yet open for adjudication.

It was clearly important in **Spector** that the courts of Connecticut had determined that the tax in that case was "placed unequivocally on the corporation's franchise for the privilege of carrying on exclusively interstate transportation in the State." In the case at bar, because Stockham was engaged within Georgia in exclusively interstate activity, the Supreme Court of Georgia followed the **Spector** decision assuming that it made no difference whether the tax is a franchise tax or a general net income tax.

We believe that the franchise tax is one channel of taxation, that the general net income tax is another, and that the latter is not merged into the former simply because a franchise tax can be measured by net income. These distinctions in terminology are meaningful and must be maintained because they are the language involved in this problem; whether they are equivalents in law is, in one sense, an issue in this case.

The starting point, as we understand it, is to find out what the General Assembly of Georgia intended to tax under Section 92-3102. Even a cursory examination of the Georgia Income Tax Act of 1931 (Ga. Laws 1931, Ex. Sess., pp. 24-60) will show that it is a general tax laid directly on income earned in Georgia. By its title it is "to provide for levying, assessing and collecting a tax on net incomes." Section 1 (Code Section 92-3101[4]) imposes the tax on the

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[3] We use the term "franchise" tax throughout this brief to include occupation, privilege or license taxes.

[4] Appendix, infra, 57.

income of individuals and Section 2 (Code Section 92-3102[5]) imposes the tax on corporations. **It is an income tax like the federal income tax.** The first Georgia income tax in 1929 (Ga. Laws 1929, pp. 92-99) even specified the levy of "an income tax similar to that of the United States"; this similarity continues in practically every provision of the Georgia income tax statutes. We want the Court to see that in the Georgia net income tax there is no trace of camouflage, subterfuge, or effort at indirection through the use of the "correct" label.

Moreover, the Georgia net income tax is no "second structure" income tax; that is, it is not a separately enacted tax on net income complementary to a franchise tax measured by net income and designed to cover taxpayers otherwise immune from the franchise tax. Concurrently with its general net income tax, Georgia does impose, under Section 92-2401[6] a franchise tax on domestic corporations, and, under Section 92-2403[7] a franchise tax on foreign corporations for the privilege of doing business in Georgia. Neither of these franchise taxes is measured by net income. The franchise tax on foreign corporations, as early as 1923, was declared unconstitutional by the Supreme Court of Georgia as applied to a foreign corporation engaged within Georgia in exclusively interstate commerce. **Dennison Manufacturing Co. v. Wright,** 156 Ga. 789, 120 S. E. 120. It has not since been applied to such corporations.

The general net income tax under Section 92-3102 is not complementary to the franchise taxes under Sections 92-2401 and 92-2403; it is imposed **in addition to and independently of** these franchise taxes. Thus, we say that the Georgia tax is a direct general net income tax, meaning that it is not by indirection a franchise, occupation, priv-

[5] Constitutional Provisions and Statutes Involved, supra, 3.

[6] Appendix, infra, 57.

[7] Appendix, infra, 57.

ilege or license tax measured by net income or intended to complement a franchise, occupation, privilege or license tax otherwise inapplicable to taxpayers engaged exclusively in interstate commerce. The taxes involved in this case were imposed as income taxes under Section 92-3102; and in nowise has Petitioner sought to impose the franchise tax under Section 92-2403 against Stockham.

Now the Supreme Court of Georgia does not deny this. It did not find, as did the Supreme Court of Connecticut in **Spector**, that the legislature intended to fix the legal incidence of the tax "unequivocally on the corporation's franchise for the privilege of carrying on exclusively interstate [commerce] within the State." Indeed, it could not because Section 92-2403 imposes such a tax, and the taxes involved here were imposed under Section 92-3102 and not under Section 92-2403. The decision of the Supreme Court of Georgia, then, does not construe Section 92-3102 to impose a franchise tax; rather, it holds, in effect, that, as a matter of law, **irrespective of legislative intent**, a general net income tax on exclusively interstate income is *per se* a franchise tax or tax on the privilege of engaging in interstate business.

This points up, we think, the crucial question whether a state tax on net income, **similar to the federal tax on income**, is *per se* a franchise, occupation, privilege or license tax requiring, for constitutional validity, that elusive factor called "a local incident," or, whether it is, in and of itself, a constitutional channel of taxation, subject only to the constitutional requirements of due process.

1. **A tax on net income is a tax on the realization of gain from property or economic activity; it is not a tax on the property or economic activity which is the source of the gain.**

It is elementary that the legal incidence of a net income tax is the realization of gain from property or economic

activity. In **Shaffer v. Carter**, 252 U. S. 37, 40 S. Ct. 221, 64 L. Ed. 445 (1920), the Court (Mr. Justice Pitney) said:

> "In a well-ordered society, property has value chiefly for what it is capable of producing, and the activities of mankind are devoted largely to making recurrent gains from the use and development of property, from tillage, mining, manufacture, from the employment of human skill and labor, or from a combination of some of these; gains capable of being devoted to their own support, and the surplus accumulated as an increase of capital. That the State, from whose laws property and business and industry derive the protection and security without which production and gainful occupation would be impossible, is debarred from exacting a share of those gains in the form of income taxes for the support of the government, is a proposition so wholly inconsistent with fundamental principles as to be refuted by its mere statement. That it may tax the land but not the crop, the tree but not the fruit, the mine or well but not the product, the business but not the profit derived from it, is wholly inadmissible.
>
> "Income taxes are a recognized method of distributing the burdens of government, favored because requiring contributions from those who realize current pecuniary benefits under the protection of the government, and because the tax may be readily proportioned to their ability to pay." (pp. 50-51)

Thus, property and activity, or a combination of the two, are the sources of income, and the gain therefrom is something different and is itself a basis of taxation.

The relationship between net income and its sources is a very basic problem in both federal and state income taxation. It is not a new problem; it ranges beyond interstate commerce and becomes involved whenever a source of income is afforded constitutional protection.

Manifestations of the problem first appeared in the relationship between net income and public salaries. In **Dobbins v. Erie County**, 16 Pet. 435, 10 L. Ed. 1022 (1842), the Court invalidated a Pennsylvania tax imposed upon the office of an officer of the United States measured by its emoluments. At that time the Court could see no difference between a tax on the office and a tax on its emoluments—both taxed an instrumentality of the United States.

Subsequently in **Collector v. Day**, 11 Wall. 113, 20 L. Ed. 122 (1871), the Court held that the federal income tax of the Civil War period could not constitutionally include income derived from compensation paid by a state because it was a tax on an instrumentality of state government.

Another manifestation of the problem appeared in 1895 in the relationship between rental income and the property producing such income. In **Pollock v. Farmers Loan & Trust Co.**, 157 U. S. 429, 15 S. Ct. 673, 39 L. Ed. 759 (1895), the Court held that the federal income tax of 1894 could not, without apportionment among the states according to population as constitutionally required for direct taxes, include rents because a tax on rents was a tax on the property which produced the rents and a direct tax. It also held that this tax could not include interest from state bonds because it was a tax on an instrumentality of government. This decision was expressly based on **Collector v. Day**; and these three decisions would seem to have established the proposition that a tax on net income **is** a tax on the source of that income.

However, a change was in the making; another manifestation of the problem appeared in 1918 in the relationship between net income and exporting. In **Peck & Co., Inc., v. Lowe**, 247 U. S. 165, 38 S. Ct. 432, 62 L. Ed. 1049 (1918), the Court held that the federal income tax did not "directly" bear on the "process of exporting" so as to be in substance a tax on exports in violation of the Constitution; the Court (Mr. Justice Van Devanter) said:

"The tax in question is unlike any of those heretofore condemned. . . . [I]t is an income tax laid generally on net incomes. . . . It is not laid on income from exportation because of its source, or in a discriminative way, but just as it is laid on other income. . . . The tax is levied after exportation is completed, after all expenses are paid and losses adjusted, and after the recipient of the income is free to use it as he chooses. Thus what is taxed—the net income—is as far removed from exportation as are articles intended for export before the exportation begins. If articles manufactured and intended for export are subject to taxation under general laws up to the time they are put in course of exportation, as we have seen they are, the conclusion is unavoidable that the net income from the venture when completed, that is to say, after the exportation and sale are fully consummated, is likewise subject to taxation under general laws." (p. 174-75)

One of the taxes theretofore condemned by the Court was a tax on the occupation of exporting, which, in **Brown v. Maryland**, 12 Wheat. 419, 6 L. Ed. 678 (1827), had been invalidated as a tax on exports. This was a significant distinction—a tax on the occupation of exporting was invalid but a tax on the income from the occupation was not.

At the same time, the Court decided **United States Glue Co. v. Town of Oak Creek**, 247 U. S. 321, 38 S. Ct. 499, 62 L. Ed. 1135 (1918), dealing with the relationship between net income and interstate commerce. The Wisconsin tax was a net income tax; about $96,000 of the taxpayer's net income had been derived from transactions strictly in interstate commerce. There can be no mistaking that the Court in that case pointed out two distinguishable lines of cases: (1) The direct (franchise and gross receipts) tax cases, and (2) the indirect (property and income) tax cases. There can be no mistaking, either, that the decision

in **U. S. Glue** was controlled by **Peck & Co.** which, as shown, was decided precisely on the relationship between income and the source of that income. It is true the United States Glue Company was a domiciliary of Wisconsin and that it was engaged in both interstate and intrastate commerce. If the legal incidence of a general tax on net income **as income** is understood, as Mr. Justice Pitney evidently understood it, these considerations are without importance. Obviously, if income is exempt from taxation because of its protected source, it is exempt whether the taxpayer is an individual or a corporation, foreign or domestic, and whether the taxpayer has other income from local sources or not. This was confirmed by the per curiam decision in **West Publishing Co. v. McColgan,** 328 U. S. 823, 66 S. Ct. 1378, 90 L. Ed. 1603 (1946), affirming the Supreme Court of California, 27 Cal. 2d 705, 166 P. 2d 861 (1946).

Thus, the decision in **Peck & Co.** and **U. S. Glue** stood together in apparent conflict with **Farmers' Loan and Trust Co.** and **Collector v. Day** on the question of the relationship between net income and the source of that income.

In 1926, in **Metcalf & Eddy v. Mitchell,** 269 U. S. 514, 46 S. Ct. 172, 70 L. Ed. 384, the Court held that the federal income tax applied to gain derived from state government contracts was not a tax on an instrumentality of government.

In 1937, in **Hale v. State Board,** 302 U. S. 95, 58 S. Ct. 102, 82 L. Ed. 72, involving the Iowa income tax and its relationship to interest on tax-exempt state bonds, the Court expressly limited **Farmers' Loan and Trust Co.** to the context of "direct" taxes under Article I, Section 2, Clause 2 of the Constitution governing the apportionment of direct taxes among the states. (See p. 107).

Then, in 1939, the coup de grace to the proposition that a tax on income is a tax on its source was administered in

Graves v. New York ex rel. O'Keefe, 306 U. S. 466, 59 S. Ct. 595, 83 L. Ed. 927, dealing with the relationship between the New York income tax and compensation paid by the federal government, wherein the Court (Mr. Justice Stone) expressly overruled **Collector v. Day**, saying:

> "The theory, which once won a qualified approval, that a tax on income is legally or economically a tax on its source is no longer tenable . . ." (p. 480)

We urge that the principle of **U. S. Glue**—that a tax on net income is not a tax on the source of that income—is not limited to the context of interstate commerce but is a manifestation of a broader principle that is a part of the warp and woof of all income taxation—state and federal.

The reiterations of this proposition in income tax cases in this country are legion. In **Shaffer v. Carter**, 252 U. S. 37, 40 S. Ct. 221, 64 L. Ed. 445 (1920), the Oklahoma income tax on a non-resident's profit from the operation of oil wells in Oklahoma was upheld against the contention that it constituted a burden on interstate commerce. There the Court (Mr. Justice Pitney) said:

> "Assuming that it fairly appears that his method of business constitutes interstate commerce, it is sufficient to say that the tax is imposed not upon the gross receipts, . . . but only upon the net proceeds, and is plainly sustainable even if it includes net gains from interstate commerce." (p. 57)

Similarly, in **Atlantic Coast Line R. Co. v. Daughton**, 262 U. S. 413, 43 S. Ct. 620, 67 L. Ed. 1051 (1923), dealing with the North Carolina income tax, the Court (Mr. Justice Brandeis) said:

> "Under the commerce clause it is essential that a state tax shall not directly burden interstate commerce and that it shall not discriminate against interstate commerce. With these essentials the North Carolina

act complies. It is not assessed on gross receipts." (p. 422)

In **New York ex rel. Cohn v. Graves**, 300 U. S. 308, 57 S. Ct. 466, 81 L. Ed. 666 (1937), the Court upheld the New York income tax against a New York resident which included rental income from property located outside New York. In so doing, the Court (Mr. Justice Stone) said:

> "Neither the privilege nor the burden is affected by the character of the source from which the income is derived. For that reason income is not necessarily clothed with the tax immunity enjoyed by its source." (p. 313)

Again, in **Wisconsin v. Minnesota Mining & Mfg. Co.**, 311 U. S. 452, 61 S. Ct. 253, 85 L. Ed. 274 (1940), the Wisconsin general corporate income tax was upheld against the contentions that it violated the commerce clause. The Court (Mr. Justice Frankfurter) said:

> "The Commerce Clause is invoked. But it is too late in the day to find offense to that Clause because a state tax is imposed on corporate net income of an interstate enterprise which is attributable to earnings within the taxing state, . . ." (p. 453)

See also, **Hans Rees' Sons v. North Carolina**, 283 U. S. 123, 51 S. Ct. 385, 75 L. Ed. 879 (1931); **Norfolk & W. Ry. Co. v. North Carolina**, 297 U. S. 682, 56 S. Ct. 625, 80 L. Ed. 977 (1936); **Helvering v. Mountain Producers Corp.**, 303 U. S. 376, 58 S. Ct. 623, 82 L. Ed. 907 (1938); **Wisconsin v. J. C. Penney Co.**, 311 U. S. 435, 61 S. Ct. 246, 85 L. Ed. 267 (1940); **International Harvester Co. v. Wisconsin**, 322 U. S. 435, 64 S. Ct. 1060, 88 L. Ed. 1373 (1944).

Thus, as we see it, the Court has unmistakably declared that a tax on net income is not a tax on the source of that income—be it property or activity. This proposition cannot be ignored; it refutes absolutely the contention that a

tax on net income from interstate commerce is a tax on interstate commerce. It is reinforced by a history of judicial travail which has run the gamut of legal argument over and over again to emerge as basic to both state and federal taxation. We think it controls this case.

2. **A general tax on net income derived exclusively from interstate commerce is neither per se a franchise tax nor per se a tax on gross receipts.**

The legal incidence of a franchise tax is the exercise of the franchise, and where particular activity is protected by the Constitution against taxation then, of course, any tax thereon is invalid. This is the holding of **M'Culloch v. Maryland**, 4 Wheat. 316, 4 L. Ed. 579 (1819), as applied to the exercise of a governmental function, **Brown v. Maryland**, 12 Wheat. 419, 6 L. Ed. 678 (1827), as applied to the occupation of exporting, **Ozark Pipe Line Corp. v. Monier**, 266 U. S. 555, 45 S. Ct. 184, 69 L. Ed. 439 (1925), **Alpha Portland Cement Co. v. Massachusetts**, 268 U. S. 203, 45 S. Ct. 477, 69 L. Ed. 916 (1925), and **Spector Motor Service, Inc., v. O'Connor**, 340 U. S. 602, 71 S. Ct. 508, 95 L. Ed. 573 (1951), as applied to interstate operations. These decisions are not, in the least, being questioned here because they, dealing with franchise taxes, have no application to a general tax imposed directly on net income.

We do not, of course, deny that "doing business" within the taxing state is a jurisdictional requirement for taxation. **Miller Bros. Co. v. Maryland**, 347 U. S. 340, 74 S. Ct. 535, 98 L. Ed. 744 (1954). But, this hardly converts every tax into a franchise tax on doing business. **Wheeling Steel Corp. v. Fox**, 298 U. S. 193, 56 S. Ct. 773, 80 L. Ed. 1143 (1936).

The contention of Respondent, however, is that a general tax imposed directly on net income is *per se* (irrespective of legislative intent) a franchise tax. If a tax on net income is not a tax on its source, as we have shown, then

a tax on net income cannot be a tax on interstate activity and a franchise tax.

The Court has repeatedly acknowledged that there are constitutional channels by which states can require interstate commerce to share in their tax burdens. The property tax is one; the highway use tax is another; and the general income tax is another. The franchise tax has never been a constitutional channel for taxing interstate commerce. Where franchise taxes upon corporations engaged in interstate commerce have been approved by the Court it has been upon finding in their operations "a local incident" (i. e., some aspect of interstate activity distinctly local). **American Mfg. Co. v. St. Louis**, 250 U. S. 459, 39 S. Ct. 522, 63 L. Ed. 1084 (1919); **Western Live Stock v. Bureau**, 303 U. S. 250, 58 S. Ct. 546, 82 L. Ed. 823 (1938). The tax in these cases was permitted to be laid upon the exercise of this "local incident"; the measure of such a tax may be some manifestation of the total enterprise standing in a causal relationship to the "local incident". **Great Atlantic & Pacific Tea Co. v. Grosjean**, 301 U. S. 412, 57 S. Ct. 772, 81 L. Ed. 1193 (1937). Only in a loose sense can it be said that this line of development has opened up a channel by which interstate commerce can be required to share in the local tax burden. It may be that Mr. Justice Stone had in mind, when writing his opinion in **Memphis Natural Gas Co. v. Beeler**, 315 U. S. 649, 62 S. Ct. 857, 86 L. Ed. 1090 (1942), that this line of development had worked itself into an equation with the net income tax as a constitutional channel of taxation; if this were true, it was undoubtedly because he found a franchise tax measured by net income like a net income tax and not because he found a net income tax like a franchise tax.

The history of the Court's dealings with franchise taxes, interstate commerce, and "a local incident" is, indeed, a "tangled underbrush of past cases". Since a tax on net

income is not a tax on the source of that income, as we have shown, these cases have no application here, and there is no more need to consider them here than for Mr. Justice Burton to have considered **U. S. Glue** in his **Spector** opinion.

Likewise, since **Fargo v. Michigan**, 121 U. S. 230, 7 S. Ct. 857, 30 L. Ed. 888 (1887), and **Philadelphia Steamship Co. v. Pennsylvania**, 122 U. S. 326, 7 S. Ct. 1118, 30 L. Ed. 1200 (1887), the Court has held that a tax on gross receipts from interstate commerce is *per se* a tax on interstate commerce. This proposition has continued as constitutional doctrine and served to invalidate the Indiana gross income tax in **Adams Mfg. Co. v. Storen**, 304 U. S. 307, 58 S. Ct. 913, 82 L. Ed. 1365 (1938), and **Freeman v. Hewit**, 329 U. S. 249, 67 S. Ct. 274, 91 L. Ed. 265 (1946).

But a general tax on net income is not converted into a tax on interstate operations simply because a tax on gross income is construed to be a tax on gross receipts. When this Court affirmed **West Publishing** in 1946 it must have rejected any contention that a net income tax was like the gross income tax declared invalid in **Adams** eight years earlier.

The evil in a gross receipts tax is its effect as a sort of duty imposed on commerce between the states. It was first condemned in **State Freight Tax Cases**, 15 Wall. 232, 21 L. Ed. 146 (1872), in the form of a tax on every ton of freight picked up for interstate carriage or delivered from interstate carriage; the Court viewed it as a duty imposed on the freight itself collected by the transportation company as a tax collector for the state. During the same term the Court approved a tax on the gross receipts from interstate transportation. **State Tax on Railway Gross Receipts**, 15 Wall. 284, 21 L. Ed. 164 (1873).

In **State Tax on Railway Gross Receipts**, the Court saw a distinction between a tax as a duty on the articles of

commerce, of which the transportation company was merely the collector, and a tax on the gross receipts of the transportation company as its own obligation. Said Mr. Justice Strong:

> "The tax is laid upon the gross receipts of the company; laid upon a fund which has become the property of the company, mingled with its other property, and possibly expended in improvements or put out at interest. . . . The tax is not levied, and, indeed such tax cannot be, until the expiration of each half-year, and until the money received for freights, and from other sources of income, has actually come into the company's hands. Then it has lost its distinctive character as freight earned, by having become incorporated into the general mass of the company's property. While it must be conceded that a tax upon interstate transportation is invalid, there seems to be no stronger reason for denying the power of a State to tax the fruits of such transportation after they have become intermingled with the general property of the carrier, than there is for denying her power to tax goods which have been imported, after their original packages have been broken, and after they have been mixed with the mass of personal property in the country." (pp. 294-95)

We know, of course, that **Fargo v. Michigan** and **Philadelphia Steamship** distinguished **State Tax on Railway Gross Receipts** and held a tax on gross receipts from interstate transportation to be invalid. The opinion of Mr. Justice Bradley, in **Philadelphia Steamship**, reveals the same ratio decidendi as the decision in **State Freight Tax Cases**:

> "Those receipts are followed and caused to be accounted for by the company, dollar for dollar. It is those specific receipts, or the amount thereof (which is the same thing), for which the company is called

upon to pay the tax. They are taxed not only because they are money, or its value, but because they were received for transportation. No doubt a ship-owner, like any other citizen, may be personally taxed for the amount of his property or estate, without regard to the source from which it was derived, whether from commerce, or banking, or other employment. But that is an entirely different thing from laying a special tax upon his receipts in a particular employment." (pp. 341-42)

Out of these cases we can see two important aspects of the Court's thinking: (1) The conception of a gross receipts tax as taking a toll or duty from every dollar of interstate commerce, and (2) the recognition that, though gross receipts epitomizes in money terms the activity which produced them, nevertheless, at some point the receipts lose identity with their source.

We think Mr. Justice Pitney, in his opinion in **U. S. Glue**, was referring to these considerations when he said:

"The difference in effect between a tax measured by gross receipts and one measured by net income, recognized by our decisions, is manifest and substantial, and it affords a convenient and workable basis of distinction between a direct and immediate burden upon the business affected and a charge that is only indirect and incidental. A tax upon gross receipts affects each transaction in proportion to its magnitude and irrespective of whether it is profitable or otherwise. Conceivably it may be sufficient to make the difference between profit and loss, or to so diminish the profit as to impede or discourage the conduct of the commerce. A tax upon the net profits has not the same deterrent effect, since it does not arise at all unless a gain is shown over and above expenses and losses, and the tax cannot be heavy unless the profits are large." (pp. 328-29)

How does changing the base of a tax from gross receipts to net income change the legal incidence of the tax? In the first place, it cannot be said that a net income tax, like a gross receipts tax, takes its toll from each and every transaction in interstate commerce as a custom collector does. The net income of a business is seldom realized ratably with each transaction; a net income tax takes no toll from the first transaction of the year, nor from the last, nor from any particular transaction during the year. Second, by reducing gross receipts by various deductions, including personal exemptions, the legislature clearly demonstrates its concern, not to tax inexorably the activity which produced the income, but to tax only increase in net worth. Some deductions, for example charitable contributions, have no connection whatever with business activity; others may have no connection with business activity within a particular state. Gain, of course, is the legal incidence of the net income tax and essential to it; but the difference between a tax on gross receipts and a tax on net income is not that the gain justifies the income tax—it is that a taxing scheme which allows for deductions demonstrates thereby beyond a doubt that the impact of the tax is not on receipts epitomizing economic activity but on realized gain itself.

Respondent's attempt to equate a net income tax with a gross receipts tax entails another important consideration. The constitutionality of the graduated income tax is well established. **Brushaber v. Union Pacific R. Co.**, 240 U. S. 1, 36 S. Ct. 236, 60 L. Ed. 493 (1916). The concept is, of course, that the net income within each bracket constitutes a separate and reasonable classification justified by its direct measure of ability to pay; the tax is solely and directly upon the income within each bracket. A graduated tax on gross receipts has been held unconstitutional by the Court in **Stewart Dry Goods Co. v. Lewis**, 294 U. S. 550, 55 S. Ct. 525, 79 L. Ed.

1054 (1935). While some doubt may be cast upon the soundness of this decision by **Great Atlantic & Pacific Tea Co. v. Grosjean**, 301 U. S. 412, 57 S. Ct. 772, 81 L. Ed. 1193 (1937), it is impossible to justify progressive rates of taxation on gross receipts by ability to pay. The justification of graduated rates of income taxation on the basis of ability to pay has been too long with us now to switch to whatever justifications exist for graduated gross receipts taxation.

3. **A tax on net income is a general tax, and, like a general property tax, does not unduly burden interstate commerce.**

We have shown that the Georgia income tax is a tax on net income **as such**, and not by indirection a tax on anything else. We have also shown that a net income tax is only remotely, and not directly, related to activity and transactions in commerce. The Georgia tax is a general tax imposed on all income "'derived from any source whatever and in whatever form paid";[8] it subjects all persons, partnerships, associations, trusts, as well as corporations to its terms; it is intended to reach only income derived from Georgia sources; it applies without discrimination to non-residents and foreign corporations as well as residents and domestic corporations, and, finally, it is a substantial source of revenue and means of distributing the costs of state government.

It might be well, at this time, to recall that the tax invalidated in **M'Culloch v. Maryland**, 4 Wheat. 316, 4 L. Ed. 579 (1819), was a tax on the operations of the Bank of the United States which was, through a private corporation, an instrumentality of the United States. Its legal incidence, then, was like the legal incidence of a

[8] Code Section 92-3107 codifying Section 10 of the Income Tax Act of 1931 (Ga. Laws 1931, Ex. Sess., p. 30).

franchise tax. For present purposes, there should be no difference in the constitutional protection afforded a private corporation which is an instrumentality of the United States and a private corporation which is an instrumentality of interstate commerce or engaged exclusively in interstate commerce. It is important to note from the opinion in **M'Culloch v. Maryland** that Mr. Chief Justice Marshall, strong Federalist though he was, took pains to point out that the decision in the case did not deprive the states of power to tax the property of the Bank.

In **Railroad Company v. Peniston**, 18 Wall. 5, 21 L. Ed. 787 (1873), following **Thomson v. Union Pacific R. Co.**, 9 Wall. 579, 19 L. Ed. 792 (1870), the Court held that the property of an agent of the United States, though a federal instrumentality, was not exempt from state taxation.

In **Peniston** the Court (Mr. Justice Strong) said:

> "In this case the tax is laid upon the property of the railroad company precisely as was the tax complained of in **Thompson v. Union Pacific**. It is not imposed upon the franchises or the right of the company to exist and perform the functions for which it was brought into being. Nor is it laid upon any act which the company has been authorized to do. It is not the transmission of dispatches, nor the transportation of United States mails, or troops, or munitions of war that is taxed, but it is exclusively the real and personal property of the agent, **taxed in common with all other property in the State of a similar character.** It is impossible to maintain that this is an interference with the exercise of any power belonging to the General government, and if it is not, it is prohibited by no constitutional implication." (p. 37; emphasis added)

Of course, the Court is right; there is no derivative immunity accorded the property of a private contractor even though used in federal service. Indeed, the Court recently

held that the tax immunity of federally-owned property is lost by its used by a private contractor. **Continental Motors Corp. v. Muskegon,** 355 U. S. 484, 78 S. Ct. 483, 2 L. Ed. 2d 436 (1958); **Detroit v. Murray Corp.,** 355 U. S. 489, 78 S. Ct. 458, 2 L. Ed. 2d 441 (1958). And there is no derivative immunity accorded the income of a private contractor derived from government contracts. **Metcalf & Eddy v. Mitchell,** 269 U. S. 514, 46 S. Ct. 172, 70 L. Ed. 384 (1926). Private corporations as instrumentalities of interstate commerce or engaged exclusively in interstate commerce should be in no better position than private contractors engaged exclusively as instrumentalities of government either with respect to state taxation of their property or of their incomes.

The Court has never deemed it necessary to protect interstate commerce from a general property tax levied upon all property within the taxing jurisdiction. In **Transportation Co. v. City of Wheeling,** 9 Otto 273, 25 L. Ed. 412 (1879), a general property tax on vessels used in interstate commerce was upheld against the contention that it was a prohibited duty on tonnage. The Court (Mr. Justice Clifford) said:

> "Annual taxes upon ships and vessels for the support of the State governments as property, upon a valuation **as other personal property,** are everywhere laid; . . ." (p. 279; emphasis added)

In **Pullman's Palace Car Co. v. Pennsylvania,** 141 U. S. 18, 11 S. Ct. 876, 35 L. Ed. 613 (1891), the Court (Mr. Justice Gray) said:

> "It is equally well settled that there is nothing in the Constitution or laws of the United States which prevents a State from taxing personal property, employed in interstate or foreign commerce, **like other personal property within its jurisdiction."** (p. 23; emphasis added)

In **Old Dominion Steamship Co. v. Virginia**, 198 U. S. 299, 25 S. Ct. 686, 49 L. Ed. 1059 (1905), a general property tax applied to a steam tug, used solely within Virginia waters but incident to exclusively interstate commerce, was upheld.

The citation of additional cases is hardly necessary; the constitutionality of a general property tax on property within a state used exclusively in interstate commerce is beyond question. These old decisions need not be recast in terms of "a local incident"; indeed, the local pick-up and delivery service involved in **Spector** did not amount to "a local incident" sufficient to justify a franchise tax, yet no one would contend, we believe, that the local pick-up and delivery trucks there were immune to a local property tax because they were involved exclusively in interstate commerce. It is not, we think, "a local incident" that qualifies property used in interstate commerce for local taxation; rather, it is (1) that a property tax is a general tax necessarily precluding any disadvantage or discrimination against interstate commerce; (2) that the incidence of a property tax, mere ownership, is only remotely related to the activity and transactions of commerce; and (3) that there is justice involved in requiring interstate commerce to pay a fair share of the local tax burden.

These considerations have been applied to a general income tax. Consider, for example, the federal income tax and the constitutional prohibition against a federal tax on exports; the income tax was upheld in **Peck & Co., Inc., v. Lowe**, 247 U. S. 165, 38 S. Ct. 432, 62 L. Ed. 1049 (1918), where the Court (Mr. Justice Van Devanter) said:

> "'[I]t is an income tax laid generally on net incomes. . . . It is not laid on income from exportation because of its source, or in a discriminative way, **but just as it is laid on other income.**": (p. 174; emphasis added)

Earlier, in **Philadelphia Steamship Co. v. Pennsylvania**, 122 U. S. 326, 7 S. Ct. 1118, 30 L. Ed. 1200 (1887), Mr. Justice Bradley, dealing with a tax on interstate gross receipts, was prompted to say:

> "Can the tax in this case be regarded as an income tax? and, if it can, does that make any difference as to its constitutionality? We do not think that it can properly be regarded as an income tax. **It is not a general tax on the incomes of all the inhabitants of the state**; but a special tax on transportation companies." (pp. 344-45; emphasis added)

The analogy between a general property tax and a general income tax in this respect was expressly drawn by Mr. Justice Pitney, in his opinion upholding the Wisconsin income tax in **U. S. Glue**, when he said:

> "Such a tax, when imposed upon net incomes from whatever source arising, is but a method of distributing the cost of government, **like a tax upon property**, or upon franchises treated as property; and if there be no discrimination against interstate commerce, either in the admeasurement of the tax or in the means adopted for enforcing it, it constitutes one of the ordinary and general burdens of government, from which persons and corporations otherwise subject to the jurisdiction of the States are not exempted by the Federal Constitution because they happen to be engaged in commerce among the States." (p. 329; emphasis added)

The decision in **U. S. Glue** was discussed from this standpoint by the late Professor Thomas Reed Powell in an article in the Harvard Law Review.[9] He concluded:

> "If the property of those engaged exclusively in interstate commerce is not exempt from state taxation,

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[9] *Indirect Encroachment on Federal Authority by the Taxing Powers of the States*, 32 Harv. L. Rev. 634 (1919).

there is no reason to accord them immunity from a tax on their net income, which is 'but a method of distributing the cost of government, like a tax upon property.' . . .

"Reason and psychology combine to warrant the expectation that the Supreme Court will not exclude foreign corporations engaged exclusively in interstate commerce from the 'corporations otherwise subject to the jurisdiction of the states' with respect to taxes on net incomes.

"It seems safe, therefore, to state the principle of the Oak Creek case by saying that a general state-wide tax on net income is not 'an unconstitutional interference with or regulation of commerce among the states' by reason of the inclusion of net income from interstate commerce. . . .

"We may take it for granted, then, that the legal character of the recipient and the nature of the business in which the recipient is engaged are immaterial elements in considering the constitutionality of a state-wide, all-inclusive general tax on net income from business done within the state. The recipient may be an individual, a partnership, a domestic or foreign corporation. The business may be exclusively interstate. But the tax must be general, and the measure must probably be net, and not gross, income . . ." (pp. 637-39)

The Georgia income tax is a general **net** income tax imposed on all income derived from sources in Georgia in the same way that its property tax is a tax on all property having a situs in Georgia; the character of the recipient and how the income is earned, like the character of the owner of property and how the property is used, are not material considerations in ascertaining its legal incidence. The power to tax net income, like the power to tax property, is original with the states; no interference with inter-

state commerce is involved; this, we submit, as constitutional doctrine which supports the Georgia income tax in this case.

B. *The Due Process Aspect.*

Of course, if a net income tax is *per se* a franchise tax, under **Spector**, the Georgia income tax is invalid, and the due process issue becomes moot. Otherwise, however, it is important for us to show that due process is satisfied.

For thirty-eight years, since 1920, the decision of the Court in **Shaffer v. Carter**, 252 U. S. 37, 40 S. Ct. 221, 64 L. Ed. 445, has stood for the proposition that a state has constitutional power to tax the income of a non-resident derived from activity within its territory. In **General Trading Co. v. State Tax Commission**, 322 U. S. 335, 64 S. Ct. 1028, 88 L. Ed. 1309 (1944), and in **International Shoe Co. v. Washington**, 326 U. S. 310, 66 S. Ct. 154, 90 L. Ed. 95 (1945), the Court indicated the quality of activity prerequisite to this power; and in **Hans Rees' Sons v. North Carolina**, 283 U. S. 123, 51 S. Ct. 385, 75 L. Ed. 879 (1931), and in **Miller Bros. Co. v. Maryland**, 347 U. S. 340, 74 S. Ct. 535, 98 L. Ed. 744 (1954), the Court has indicated limitations on this power.

The stipulated facts show that Stockham was definitely physically present and engaged in business within Georgia during the tax years in question. Its presence and activity was no casual, transitory, spasmodic, traveling-drummer type of activity; Stockham was permanently, regularly and competitively engaged in business within Georgia, even though it was entirely pursuant to interstate commerce.

The Supreme Court of Georgia by its reference (R. 36) to its decision in **Redwine v. Dan River Mills**, 207 Ga. 381, 61 S. E. 2d 771 (1950), and **Suttles v. Owens-Illinois Glass Co.**, 206 Ga. 849, 59 S. E. 2d 392 (1950), apparently takes the "minimum connections," referred to in **Miller Bros.**, to require at least some transactions within the taxing state,

such as the contractual consummation of a sale or the actual delivery of goods from inventory, and to ignore other activity, no matter how substantial, which does not culminate within the taxing state in some such transactions. The amendment of 1950 to Section 92-3113 purposely used the term "activities or transactions" in its definition of "doing business" to expand it beyond transactions alone and to exhaust the State's constitutional power to tax on the basis of activities within the State as well as transactions. The effect of the decision of the Supreme Court of Georgia is to say that the due process clause of the Fourteenth Amendment precludes activities other than those culminating in some transactions within the state from giving jurisdiction to tax and to ignore such activities in deciding whether the state has given any protection, opportunities and benefits for which it can reasonably demand a tax.

Such a concept of the constitutional scope of "doing business" is too narrow. Modern business being what it is, there are many important business activities which involve no contractual transactions and which make substantial contributions to the production of income; many illustrations come to mind: a research center, an advertising department, a consumer research division, a dealer training program, etc. Any one of these could be carried on within a state with no more than an office or a laboratory and one or a few employees and be a substantial factor in the production of income.

This Court, we believe, has adopted the broader view of the matter. It is significant to note that in **West Publishing** this Court cited **International Shoe** which in turn cited **General Trading**, which in turn cited **Felt & Tarrant Mfg. Co. v. Gallagher**, 306 U. S. 62 (1939), and **Nelson v. Sears, Roebuck & Co.**, 312 U. S. 359 (1941); a review of these cases will show that solicitation and other sales service activities, **conducted on a continuous, designed and competitive**

basis, are enough to satisfy due process irrespective of contractual transactions within the taxing state.

1. Due process does not prohibit the taxation of income of a non-resident earned within the taxing state.

It is not questioned that a state may impose a net income tax upon income earned by non-residents within the taxing state. This was settled in **Shaffer v. Carter,** 252 U. S. 37, 40 S. Ct. 221, 64 L. Ed. 445 (1920). The "radical contention" that the state could not impose such a tax without violating due process was answered by the Court in **Shaffer v. Carter** by reference to "fundamental principles." These fundamental principles are that a state in which a corporation owns property or engages in business activities confers certain benefits and protection upon the corporation and has, in return, the right to impose taxes upon such corporation to help defray the expenses of government. It is not necessary that the corporation have any tangible property in the taxing state. In **New York ex rel. Whitney v. Graves,** 299 U. S. 366, 57 S. Ct. 237, 81 L. Ed. 285 (1937), the Court upheld a New York tax upon the income derived by a Massachusetts resident from the sale of a right to purchase part of a seat on the New York Stock Exchange.

2. Due process, for in personam jurisdictional purposes, requires only "minimum connections" with the state seeking jurisdiction.

The law concerning jurisdiction of a state over a foreign corporation has gone through considerable evolution since **Bank of Augusta v. Earle,** 13 Pet. 519, 10 L. Ed. 274 (1839). It was then accepted constitutional doctrine that a corporation could not be "present" in any state except the state of incorporation and, therefore, was not subject to the jurisdiction of any other state under any circumstances. It was believed that a corporation could be present only in the state of its incorporation because

it was purely a creature of law and, since the laws of a state are limited to the territorial limits of the state, the life-force of a corporation was necessarily limited to the state which created it.

Of course, this soon proved unsatisfactory, so the Court indulged in a fictional consent or submission to the jurisdiction of a foreign state. **Lafayette Ins. Co. v. French**, 18 How. 404, 15 L. Ed. 451 (1855).

In modern times neither "presence" nor "consent" is the basis of jurisdiction over foreign corporations. As early as 1930 in **Hutchinson v. Chase & Gilbert**, C. C. A. 2d, 45 F. 2d 139, Judge Learned Hand said:

> "It is difficult, to us it seems impossible, to impute the idea of locality to a corporation, except by virtue of those acts which realize its purposes." (p. 141)

In other words, jurisdiction over a foreign corporation is not determined circuitously by reference to its "presence" or "consent", but directly by reference to the purposeful activity of its agents and employees within the state seeking jurisdiction. This idea was adopted completely by **International Shoe Co. v. Washington**, 326 U. S. 310, 66 S. Ct. 154, 90 L. Ed. 95 (1945), where the Court (Mr. Chief Justice Stone for a unanimous Court, Mr. Justice Jackson not participating) said:

> "Since the corporate personality is a fiction, . . . it is clear that unlike an individual its 'presence' without, as well as within, the state of its origin can be manifested only by activities carried on in its behalf by those who are authorized to act for it." (p. 316)

Express judicial cognizance of these developments was taken recently in **McGee v. International Life Ins. Co.**, 355 U. S. 220, 78 S. Ct. 199, 2 L. Ed. 2d 223 (1957), where the Court (Mr. Justice Black for a unanimous Court, Mr. Chief Justice Warren not participating) said:

> "In a continuing process of evolution this Court accepted and then abandoned 'consent,' 'doing business,' and 'presence' as the standard for measuring the extent of state judicial power over [foreign] corporations." (p. 222)

The best expression of the test came in **Miller Bros. Co. v. Maryland**, 347 U. S. 340, 74 S. Ct. 535, 98 L. Ed. 744 (1954), when the Court (Mr. Justice Jackson) said:

> "But the course of decisions does reflect at least consistent adherence to one time-honored concept: that due process requires some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax." (pp. 344-45)

Thus, "presence" has been discarded and the inquiry is directed straight to the due process criterion: are there "minimum connections" between the foreign corporation and the state seeking jurisdiction over the corporation?

3. **The continuous, designed and competitive exploitation of the markets of a taxing state constitutes sufficient connections to satisfy due process.**

Before making any further analysis of the concept of "minimum connections" it might be well to point out several overriding propositions. The first is that actual contacts with a state are not disembodied by reason of being exclusively in interstate commerce. Such a contention was made in **International Harvester Co. v. Kentucky**, 234 U. S. 579, 34 S. Ct. 944, 58 L. Ed. 1479 (1914), but was deemed "novel" and explicitly rejected; it was also rejected in **West Publishing Co. v. McColgan**, 27 Cal. 2d 705, 166 P. 2d 861 (1946), affirmed per curiam 328 U. S. 823, 66 S. Ct. 1378, 90 L. Ed. 1603 (1946). In other words, Stockham's activities within Georgia, as stipulated, were not any less activities within Georgia because they were exclusively in interstate commerce.

The second is that what constitutes "minimum connections" for purposes of in personam jurisdiction also constitutes "minimum connections" for purposes of taxation. In **International Shoe** the Court (Mr. Chief Justice Stone) said:

> "The activities which establish its 'presence' subject it alike to taxation by the state and to suit to recover the tax." (p. 321)

The third is that it is the **quality** of these contacts and not necessarily the quantity that controls. Again, in **International Shoe**, it was said:

> "The test is not merely, as has sometimes been suggested, whether the activity, which the corporation has seen fit to procure through its agents in another state, is a little more or a little less. [citations omitted] Whether due process is satisfied must depend rather upon the quality and nature of the activity in relation to the fair and orderly administration of the laws which it was the purpose of the due process clause to insure." (p. 319).

As we shall point out later, a fair apportionment statute measures the quantity of a taxpayer's activity within the taxing state. If the activity is great, the apportionment will be great; if the activity is small, the apportionment will be small. Respondent does not challenge the fairness of the Georgia apportionment statute; hence, no question of the quantity of its activity within this state is involved.

Considerable light is thrown on the content of the "minimum connections" concept by a comparison of the facts involved in two cases decided by the Court. In **Miller Bros. Co. v. Maryland**, 347 U. S. 340, 74 S. Ct. 535, 98 L. Ed. 744 (1954), Maryland sought to require a foreign corporation to collect its use tax on sales made in Delaware to residents of Maryland. Maryland's assertion of jurisdic-

tion was held to violate due process because the contacts of the corporation with Maryland were not sufficient; there was no regular activity in Maryland, only the occasional delivery of goods purchased in Delaware.

However, in **General Trading Co. v. State Tax Commission**, 322 U. S. 335, 64 S. Ct. 1028, 88 L. Ed. 1309 (1944), the Court upheld the effort of Iowa to compel a Minnesota corporation to collect its use tax on sales made in Minnesota to Iowa residents. In that case the Minnesota corporation sent its agents from its Minnesota headquarters into Iowa to procure business from Iowa residents in such manner as to be treated as maintaining a place of business in Iowa. Mr. Justice Jackson, in **Miller Bros.** compared **General Trading** in this way:

> "The Court could properly approve the State's decision to regard such rivalry with its local merchants as equivalent to being a local merchant. But there is a wide gulf between this type of active and aggressive operation within a taxing state and the occasional delivery of goods sold at an out-of-state store with no solicitation other than the incidental effects of general advertising." (pp. 346-47)

We are led by a consideration of these cases to the conclusion that the required "minimum connections" is determined by the foreign corporation's pattern of conduct manifesting its designs on the markets of the taxing state.

The days of laissez-faire are gone, and government expenditure for the promotion of a healthy and attractive economy is not limited to the federal government. State governments, too, spend tax monies to develop their economies and provide the necessary services required therewith. There is certainly justice and fairness in requiring foreign corporations to share, through taxation, in the costs of state government when such corporations engage

in a pattern of conduct, continuously, designedly and competitively, to get all the business it possibly can out of a state's economy, using the same methods as local taxpaying competitors.

Consider Stockham's pattern of conduct and designs on the markets of Georgia. It had an established and publicly-identified office in Atlanta (R. 5) with a full-time resident representative who operated out of that office and made every effort to procure for Stockham as much business in Georgia as he could (R. 6). Stockham also employed a secretary in the Atlanta office who was in instantaneous communication with the main office in Birmingham (R. 5). This and the proximity of Birmingham to Georgia were important to Stockham because it could and did represent to prospective customers in Georgia that its service was the equivalent of local service (R. 7). Admittedly the purpose of this was to place Stockham in a position so that it could compete equally with local merchants (R. 5). The facts are that Stockham's every effort was to compete successfully in Georgia and garner as much of the Georgia market for valves and fittings as it possibly could, save only this: it was meticulous to avoid any semblance of "local activity" because it hoped thereby to escape taxation in Georgia. But the pattern of its activities in Georgia was systematic, continuous and designed; the words "occasional" and "incidental" used by the Court in describing the activity of Miller Brothers in Maryland are by no means appropriate to describe Stockham's connections with Georgia.

The activities of International Harvester in Kentucky, as described in **International Harvester Co. v. Kentucky**, 234 U. S. 579, 34 S. Ct. 944, 58 L. Ed. 1479 (1914), were very similar to the activities of Stockham in Georgia. There a definite effort was made by the company to insure that all activities in Kentucky were exclusively interstate.

The usual precautions were taken: all orders were accepted at an office outside the State; title to all shipments passed outside the State; agents in Kentucky had no discretion whatsoever, so that about all they did was solicit business in the State. Stockham was just as careful to see that its activities in Georgia remained exclusively interstate; to this end it denied to its Georgia representative the authority, contractually, to accept orders for goods (R. 4, 7); it completed all sales by deliveries to carriers outside Georgia (R. 5); it never qualified to do business in Georgia (R. 8). Unlike International Harvester, Stockham did maintain an office in Georgia, advertised the presence of the office on its letterheads, catalogues, discount sheets and sales promotional material and promoted it as the equivalent of local service (R. 5).

The Court held that International Harvester was subject to the jurisdiction of Kentucky as a criminal defendant. It was emphasized that the company was engaged in a continuous course of business, not isolated transactions. The company argued that it was engaged exclusively in solicitation of interstate commerce, and that this was not enough to confer jurisdiction; the Court replied that a **continuous** course of solicitation followed by delivery of goods into the State plus authority to receive payment was sufficient.

After the decision of the Court in **McGee v. International Ins. Company,** 355 U. S. 220, 78 S. Ct. 199, 2 L. Ed. 2d 223 (1957), it would appear beyond question that any regular, continuous, systematic, designed, competitive business activity carried on within a state is sufficient to give that state jurisdiction over a foreign corporation. It is not indispensable that a foreign corporation maintain an office in a state in order for that state to obtain jurisdiction over it. **General Trading Co. v. State Tax Commission,** 322 U. S. 335, 64 S. Ct. 1028, 88 L. Ed. 1309 (1944). If a foreign cor-

poration does maintain an established office in a state, that fact alone is conclusive of jurisdiction over the corporation. The decision in **Cheney Brothers Co. v. Massachusetts**, 246 U. S. 147, 38 S. Ct. 295, 62 L. Ed. 632 (1918), does not contradict this proposition because the Massachusetts tax there was a franchise tax and held to be a tax on exclusively interstate commerce; in **Northwestern Consolidated Milling Co.**, decided in the same reported decision, due process was held satisfied by activity of solicitors less substantial in its quality than that of Stockham in Atlanta.

4. **Due process also requires, for income taxing purposes, that the income have a situs or source within and limited to the taxing state.**

This is a second requirement of due process independent of "minimum connections" and domiciliary jurisdiction. For example, in **Union Refrigerator Transit Co. v. Kentucky**, 199 U. S. 194, 26 S. Ct. 36, 50 L. Ed. 150 (1905), Kentucky was prohibited by due process from imposing a property tax on all property of a domiciliary corporation. In **Mexican Petroleum Corp. v. Head**, 64 Ga. App. 529, 13 S. E. 2d 887 (1941), the State of Georgia was not permitted to tax the income of a Georgia corporation realized from a separate and disconnected phase of its business carried on in New York; while the decision was based on statutory construction, the Georgia Court of Appeals definitely thought that the decision in **Hans Rees' Sons v. North Carolina**, 283 U. S. 123, 51 S. Ct. 385, 75 L. Ed. 879 (1931), precluded taxation of income derived from sources outside the taxing state.

The difference between these two aspects of due process can be seen in **Connecticut General Life Ins. Co. v. Johnson**, 303 U. S. 77, 58 S. Ct. 436, 82 L. Ed. 673 (1938). The question there was not whether California had jurisdiction to tax the corporation; this was conceded by the corporation because of its admission to do business in California.

The issue was whether California could tax receipts earned from reinsurance contracts made outside the state and handled completely outside the state. This shows a second due process question, that of measuring a tax, otherwise jurisdictionally imposed, by extraterritorial values. The difference was made clear in **Braniff Airways, Inc., v. Nebraska**, 347 U. S. 590, 74 S. Ct. 757, 98 L. Ed. 967 (1954). The activity of Braniff in landing planes regularly in Nebraska gave the company sufficient contacts with the state to justify imposing a tax, but there was the further question whether the tax was measured by extraterritorial values.

Domicile, of course, gives a state jurisdiction to impose a tax on its domiciliary, and performs the same function as is performed in the case of a foreign corporation by "minimum connections". But, the fact that a person is domiciled in a state when he dies does not give that state the right to impose a death tax upon the transfer of his property which has acquired a permanent situs in another state. That was settled in **Frick v. Pennsylvania**, 268 U. S. 473, 45 S. Ct. 603, 69 L. Ed. 1058 (1925). There was no question of the jurisdiction of Pennsylvania over Frick's estate, but the tax could not be imposed upon the full value of his estate because that involved extraterritorial values.

It was made clear in **Hans Rees' Sons** that an income tax which taxes extraterritorial values violates due process. And the teaching of that case is that a state, otherwise having jurisdiction, can impose its income tax only on income having a situs or source within the taxing state.

There is nothing strange in saying that income has a situs. It is self-evident in a simple context. Suppose, for example, a foreign corporation engages in no activity within Georgia but owns a piece of unimproved realty which it sells at a gain; no one, we believe, would deny

that this gain has a situs in Georgia. On the other hand, suppose this foreign corporation owns bonds of a Georgia corporation which it sells at a gain; the source of the gain being intangible property having a situs at the domicile of the owner, so would the situs of this gain be at the domicile of the owner.

An examination of the further provisions of Code Section 92-3113 shows that it proceeds on the premise that gain has a situs according to the situs of its source.[10]

A judicial expression of this idea is to be found in **State ex rel. Manitowac Gas Co. v. Wisconsin**, 161 Wisc. 111, 152 N. W. 848 (1915), where the Supreme Court of Wisconsin said:

> "If an income be taxed the recipient thereof must have a domicile within the state, or the property or business out of which the income issues must be situated within the state so that the income may be said to have a situs therein. . . .
>
> "The income tax law does not seek to reach property or an interest in property as such, but to reach incomes having a situs within the state or growing out of a privilege exercised or occupation conducted within the state." (pp. 114-15)

That Court invalidated the Wisconsin income tax as applied to the bond-interest income of a non-resident saying:

> "The situs of the property out of which such income issues is that of the domicile of the creditor. . . . So the interest in question did not . . . constitute an income from sources within the state. . . ." (p. 115)

The determination of a taxable situs for income is not unlike the determination of a taxable situs for property. In the absence of proof of activity in other states sufficient

[10] See Appendix, infra, 57.

to indicate a situs there, it makes sense to consider the situs of income at the recipient's domicile or principal place of business. **Compania General de Tabacos de Filipinas v. Collector**, 279 U. S. 306, 49 S. Ct. 304, 73 L. Ed. 704 (1929); compare **Northwest Airlines, Inc., v. Minnesota**, 322 U. S. 292, 64 S. Ct. 950, 88 L. Ed. 1283 (1944). But, given activity within and without the state of domicile or principal place of business the problem is not so easily solved.

5. **A fair apportionment statute reflects income having a situs or source within the taxing state and precludes the taxation of income having a situs or source outside the taxing state.**

Ascertaining the situs of gain from specific transactions at a particular place is one thing; ascertaining the situs of gain from a business conducted over several states is another and presents a more difficult problem because the source of that gain is activity which ignores or transcends territorial boundaries. Business activity, however, in a simple context, self-evidently has a locale or situs similar to the situs of property; and the income derived therefrom, too, has a situs which is co-extensive with the activity that produced it. Multi-state business activity has no less a situs because of the difficulties of actual allocation; the resort to formula allocation or apportionment is not a resort to abstraction but, rather, is a method of measuring concrete activity which because of its subtle manifestations and complex interactions is otherwise impossible of measurement and allocation.

The purpose of an apportionment formula was declared by the Court in **Underwood Typewriter Co. v. Chamberlain**, 254 U. S. 113, 41 S. Ct. 45, 65 L. Ed. 165 (1920):

> "The profits of the corporation were largely earned by a series of transactions beginning with manufacture

in Connecticut and ending with sale in other States. In this it was typical of a large part of the manufacturing business conducted in the State. The legislature in attempting to put upon this business its fair share of the burden of taxation was faced with the impossibility of allocating specifically the profits earned by the processes conducted within its borders. It, therefore, adopted a method of apportionment which, for all that appears in this record, reached, and was meant to reach, only the profits earned within the State." (pp. 120-21)

The Court is, of course, familiar with the use of apportionment formulas. E. g., **Pullman's Palace Car Co. v. Pennsylvania,** 141 U. S. 18, 11 S. Ct. 876, 35 L. Ed. 613 (1891). Their use has generated much litigation and no purpose will be served by reviewing it at this time. It ought to be sufficient that a formula similar to the one applied against Stockham in this case was approved by the Court as to due process in **Butler Bros. v. McColgan,** 315 U. S. 501, 62 S. Ct. 701, 86 L. Ed. 991 (1942), where Mr. Justice Douglas, speaking for a unanimous Court, said:

"We read the statute as calling for a method of allocation which is 'fairly calculated' to assign to California that portion of the net income 'reasonably attributable' to the business done there. The test, not here challenged, which has been reflected in prior decisions of this Court, is certainly not more exacting. [citations omitted] Hence, if the formula which was employed meets those standards, any constitutional question arising under the Fourteenth Amendment is at an end." (pp. 506-507)

In **Ott v. Mississippi Valley Barge Line Co.,** 336 U. S. 169, 69 S. Ct. 432; 93 L. Ed. 585 (1949), the Court (Mr. Justice Douglas) said:

"So far as due process is concerned the only question is whether the tax in practical operation has

relation to opportunities, benefits, or protection conferred or afforded by the taxing State. [citations omitted] Those requirements are satisfied if the tax is fairly apportioned to the commerce carried on within the State." (p. 174)

This same proposition was reaffirmed in **Braniff Airways, Inc., v. Nebraska,** 347 U. S. 590, 74 S. Ct. 757, 98 L. Ed. 967 (1954).

All of which is to say, as we see it, that the function of an apportionment formula in the due process context is not with respect to "minimum connections"; its use assumes that the "minimum connections" requirement of due process is satisfied and it proceeds to fix, what is known to exist but is impossible of direct proof, the situs of income; and when income is shown to have a situs at a certain place it necessarily follows that the recipient of that income has been afforded "opportunities, benefits or protection" at that place.

C. The Multiple Burdens Aspect.

Stockham has raised the traditional contention of those engaged in interstate operations that interstate commerce, because it is interstate commerce, is exposed to multiple burdens of taxation not borne by local commerce. It was, the argument runs, the intent of the founding fathers, and is now the very purpose of the commerce clause to prevent the confronting of interstate operators with a "balkanized" array of states, each to be dealt with separately, etc.

Of course, all we have said with respect to the interstate commerce aspect of this case is directed against this argument. To be sure, the commerce clause creates an area of free trade **but,** as we have shown, in taxation, it is only with respect to direct burdens—franchise and gross receipts taxes—that this area of immunity exists; it does not exist with respect to general property taxes or general in-

come taxes which stand in no direct relation to the activities of property owners or recipients of income. It goes without saying that much of the work of the Court since its beginning has been to reconcile the acknowledged justice in having interstate commerce share in the tax burdens of the states in which it operates with the purpose of the commerce clause. The argument against "balkanization," if it means absolutely no state taxes on those engaged in interstate commerce and as instrumentalities of interstate commerce, is so manifestly unjust in the federal-state relationship as to refute itself.

This Court's concern with multiple taxes on interstate commerce long antedated **Western Live Stock v. Bureau,** 303 U. S. 250, 58 S. Ct. 546, 82 L. Ed. 823 (1938). Indeed, it is clear from Mr. Justice Stone's opinion that he thought the basic reason for the condemnation of franchise and gross receipts taxes was the incipiency of multiple taxation inherent in the situation; his equation of the threat of multiple taxation with the direct taxation previously condemned by the Court was an effort to narrow, not broaden, the immunity of interstate commerce from state taxation. It was clearly his idea that a situation of no-threat of multiple taxation would validate any form of state taxation; this was rejected in **Spector**. The point, of course, is that all of this development was aimed at relaxing the interstate commerce immunity from franchise and gross receipts taxes and, in no wise, at developing a new argument for extending the immunity to property and income taxes.

1. The threat of a second income tax at taxpayer's domicile merely raises the long-time question of whether due process prohibits more than a single situs for the taxation of income; it does not.

Stockham has contended that subjecting its entire net income to taxation, though fairly apportioned among all the states in which it operates, exposes its entire net in-

come to a second tax in that its entire net income is also subject to taxation by the state of its domicile or principal place of business.

As shown, the threat of multiple taxation under the commerce clause assumes that a franchise or gross receipts tax is involved; it is one of the reasons for condemning franchise and gross receipts taxes on interstate commerce and not a reason for condemning property or net income taxes which fall upon those engaged in interstate commerce.

In **Shaffer v. Carter**, 252 U. S. 37, 40 S. Ct. 221, 64 L. Ed. 445 (1920), the Court unequivocally upheld the right of a state to impose its income tax upon a non-resident's income derived from sources within the state. This was against the contention that, under due process, the income could only be taxed at the state of the taxpayer's domicile.

Subsequently, in **Lawrence v. State Tax Commission**, 286 U. S. 276, 52 S. Ct. 556, 76 L. Ed. 1102 (1932), the Court held that, under due process, the state of domicile could tax the entire net income of its residents wherever earned.

Of course, **Lawrence** was not decided in ignorance of what had been decided in **Shaffer v. Carter**. Indeed, the decision, for purposes of taxable situs under due process, equated a tax on income with a tax on intangible property when it rejected the application of **Union Refrigerator Transit Co. v. Kentucky**, 199 U. S. 194, 26 S. Ct. 36, 50 L. Ed. 150 (1905), and **Frick v. Pennsylvania**, 268 U. S. 473, 45 S. Ct. 603, 69 L. Ed. 1058 (1925).

Due process does not prohibit more than a single situs for purposes of taxing intangible property. **Wheeling Steel Corp. v. Fox**, 298 U. S. 193, 56 S. Ct. 773, 80 L. Ed. 1143 (1936); **Curry v. McCanless**, 307 U. S. 357, 59 S. Ct. 900, 83 L. Ed. 1339 (1939); **State Tax Commission v. Aldrich**, 316 U. S. 174, 62 S. Ct. 1008, 86 L. Ed. 1358 (1942).

Although the Court in its decision in **Lawrence** created the prospect of multiple taxation of income, it, at the same time, decided that due process is not violated thereby.

2. **If the commerce clause prohibits more than an apportioned tax on the total net income derived from interstate commerce the state of domicile or principal office would be required to yield to the state or states of the source.**

The Court in **Standard Oil Co. v. Peck**, 342 U. S. 382, 72 S. Ct. 309, 96 L. Ed. 427 (1952), indicated that the commerce clause does prohibit more than an apportioned tax on the total movable property of an instrumentality of commerce. There the Court (Mr. Justice Douglas) said:

> "The rule which permits taxation by two or more states on an apportionment basis precludes taxation of all the property by the state of the domicile. [citations omitted] Otherwise there would be multiple taxation of interstate operations and the tax would have no relation to the opportunities, benefits, or protection which the taxing state gives those operations." (pp. 384-85)

It may be that this, as applied to an income tax, throws doubt upon **Lawrence** and makes it now uncertain whether income will be dealt with as analogous to intangible property as in that case, or as analogous to movable tangible property as in **Standard Oil Co. v. Peck.** In either event, there is no question as to the right of the state of the source of income to tax, which is the right under which the State of Georgia claims jurisdiction to tax an apportioned part of Respondent's net income in this case.

3. **As among states from which income is derived, a fair apportionment formula precludes multiple taxation of the total net income.**

The use of apportionment formulas to effect a fair administration of state taxing laws as required by due proc-

ess is long and well established in both property taxation, **Pullman's Palace Car Co. v. Pennsylvania**, 141 U. S. 18, 11 S. Ct. 876, 35 L. Ed. 613 (1891); **Ott v. Mississippi Valley Barge Line Co.**, 336 U. S. 169, 69 S. Ct. 432, 93 L. Ed. 585 (1949); and **Braniff Airways, Inc., v. Nebraska**, 347 U. S. 590, 74 S. Ct. 757, 98 L. Ed. 967 (1954); and income taxation, **Underwood Typewriter Co. v. Chamberlain**, 254 U. S. 113, 41 S. Ct. 45, 65 L. Ed. 165 (1920); **Butler Bros. v. McColgan**, 315 U. S. 501, 62 S. Ct. 701, 86 L. Ed. 991 (1942).

Manifestly, it is logically impossible to have the same income taxed twice when all portions cannot exceed the whole. Practically it could happen for two reasons: (1) Apportionment formulas are only prima facie fair and the burden is upon the taxpayer to plead and prove their unfairness; conceivably, then, more than 100% could be subjected to income taxation because of the failure of the taxpayer to carry this burden. (2) The make-ups of apportionment formulas used by the various income-taxing states may, and do, vary; this conceivably can produce, in some degree, multiple taxation of the same income, but uniformity along this line among the several states is a matter for legislative, not judicial solution.

Taxation, it has been said, is a practical matter. Taxpayers have protection under **Hans Rees' Sons v. North Carolina**, 283 U. S. 123, 51 S. Ct. 385, 75 L. Ed. 879 (1931), from an apportionment formula which fails to give full consideration to important income-producing factors. It may be that formula uniformity among income-taxing states is a desirable thing. The National Tax Association has been working for years on such a project. However, the nature of the problem, with all of its complexities, suggests that any solution of this type ought to come from Congress. In some respects the problem is similar to the problem of taxing national banks. For years Congress has regulated state taxation of national banks and offered to

the states certain optional methods of taxation.[11] Until the problem becomes serious enough to warrant Congressional action, the rule of apportionment, as authorized and limited by the Court over the years since **Pullman's Palace Car**, seems adequate.

4. The burden of keeping records and filing returns as required by the laws of the various states in which income is derived is no more than an incidental burden on interstate commerce.

Stockham has also complained of the burden which falls upon those engaged in interstate commerce with respect to keeping records and filing returns in the numerous jurisdictions over the entire United States which have authority to and do impose taxes on net incomes.

Undoubtedly it is an inconvenience and expense to comply with the different laws, tax and otherwise, of the various states and political subdivisions in which a nation-wide enterprise chooses to do business. We do not hesitate to admit that in economic burden the Georgia income tax is actually something in excess of the statutory four per cent. rate. However, the Court has made it clear that it is not the economic burden on interstate commerce which determines invalidity under the commerce clause. As the Court said in **Spector**:

> "Even though the financial burden on interstate commerce might be the same, the question whether a state may validly make interstate commerce pay its way depends first of all upon the constitutional channel through which it attempts to do so" (p. 608).

Since a net income tax is a constitutional channel, the incidental expense entailed in having to keep appropriate records and file returns is hardly enough to make it a direct burden which the commerce clause forbids.

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[11] Beginning with the National Bank Act, 13 Stat. 111 (1864); presently codified, as amended, in 12 U. S. C., § 548.

CONCLUSION.

Petitioner believes that every contention of Respondent is answered by the combination of **United States Glue Co. v. Town of Oak Creek**, 247 U. S. 321, 38 S. Ct. 499, 62 L. Ed. 1135 (1918); **West Publishing Co. v. McColgan**, 328 U. S. 823, 66 S. Ct. 1378, 90 L. Ed. 1603 (1946), affirming per curiam the Supreme Court of California, 27 Cal. 2d 705, 166 P. 2d 861 (1946); **Shaffer v. Carter**, 252 U. S. 37, 40 S. Ct. 221, 64 L. Ed. 445 (1920); **International Shoe Co. v. Washington**, 326 U. S. 310, 66 S. Ct. 154, 90 L. Ed. 95 (1945), and **Butler Bros. v. McColgan**, 315 U. S. 501, 67 S. Ct. 701, 86 L. Ed. 991 (1942). More particularly, all contentions advanced by Respondent were answered in one decision by the Supreme Court of California in its **West Publishing** decision, which this Court affirmed per curiam.

It is true that the tax involved in **West Publishing** was a "second structure" income tax, that is, a separately enacted tax on net income complementary to a franchise tax measured by net income and designed to cover taxpayers otherwise immune from the franchise tax. The Georgia income tax, as shown, is not a "second structure" income tax. Whether a "second structure" income tax should be accorded treatment as a general net income tax or treatment as a franchise tax is before this Court in other cases but not in this case. This much is clear: the "second structure" tax involved in **West Publishing** was treated by both this Court and the Supreme Court of California as a general net income tax.

It has been the purpose of our argument to show that **West Publishing**, with respect to a general net income tax, was soundly decided on principles basic to income taxation, and was in nowise dependent upon the dictum of Mr. Justice Stone in **Memphis Natural Gas Co. v. Beeler**, 315 U. S. 649, 62 S. Ct. 857, 86 L. Ed. 1090 (1942), which was re-

jected in footnote 6 of the majority opinion in **Spector Motor Service, Inc., v. O'Connor**, 340 U. S. 602, 71 S. Ct. 508, 95 L. Ed. 573 (1951).

Indeed, **Spector** is no departure from established doctrine; it is but a more modern counterpart of **Ozark Pipe Line Corp. v. Monier**, 266 U. S. 555, 45 S. Ct. 184, 69 L. Ed. 439 (1925), and **Alpha Portland Cement Co. v. Massachusetts**, 268 U. S. 203, 45 S. Ct. 477, 69 L. Ed. 916 (1925), both of which were decided after **U. S. Glue** and before **West Publishing** and have had no such effect as is contended here should follow from **Spector**. In **Alpha Portland Cement**, Mr. Justice McReynolds said:

> "The right to lay taxes on tangible property or on income is not involved; . . ." (p. 216)

His answer then is our answer now to any contentions that **Spector** has changed constitutional doctrine with respect to a general income tax. The real significance of **Spector** is that it did not change constitutional doctrine; the development begun by Mr. Justice Stone to convert the franchise tax into a constitutional channel of taxation on interstate commerce like the general income tax was stopped short by that decision.

The general income tax is a basic source of revenue for many states as it is for the federal government; at the state level, it has largely supplanted the general property tax. This Court, for forty years, has recognized it as a constitutional channel by which states can require interstate commerce to pay a fair share of the expenses of state government; this recognition stems from basic principles of income taxation altogether different from principles of franchise taxation. There are problems, to be sure, but the effort of the states to raise revenue by means of a general income tax ought to be spared the "tangled underbrush of past decisions" which has characterized franchise taxation.

A reversal of the decision of the Supreme Court of Georgia is respectfully requested.

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APPENDIX.

1. **Section 92-3101 of the Code of Georgia of 1933**, the same being also Section 3 of the Income Tax Act of 1931 (Ga. Laws 1931, Ex. Sess., pp. 24, 26), as amended and in effect during the years involved in this case:

> **Rate of taxation of individuals.**—A tax is hereby imposed upon every resident of this State, which tax shall be levied, collected and paid annually with respect to the entire net income of the taxpayer as hereinafter defined; and upon every non-resident with respect to his entire net income not hereinafter exempted, received by such taxpayer from property owned or from business carried on in this State; computed at the following rates:

2. **Section 92-3113 of the Code of Georgia of 1933**, the same being also Section 15 of the Income Tax Act of 1931 (Ga. Laws 1931, Ex. Sess., pp. 24, 34-36), as amended (Ga. Laws 1950, pp. 299, 300-303) and in effect during the years involved in this case:

> **Corporations, allocation and apportionment of income.**—The tax imposed by this law shall apply to the entire net income, as herein defined, received by every corporation, foreign or domestic, owning property or doing business in this State. Every such corporation shall be deemed to be doing business within this State if it engages within this State in any activities or transactions for the purpose of financial profit or gain, whether or not such corporation qualifies to do business in this State, and whether or not it maintains an office or place of doing business within this State, and whether or not any such activity or transaction is connected with interstate or foreign commerce.

If the entire business income of the corporation is derived from property owned or business done in this State, the tax shall be imposed on the entire business income, but if the business income of the corporation is derived in part from property owned or business done in the State and in part from property owned or business done without the State, the tax shall be imposed only on that portion of the business income which is reasonably attributable to the property owned and business done within the State, to be determined as follows:

(1) Interest received on bonds held for investment and income received from other intangible property held for investment are not subject to apportionment. Rentals received from real estate held purely for investment purposes and not used in the operation of the business are also not subject to apportionment. All expenses connected with the interest and rentals realized from such investments are likewise not subject to apportionment but must be applied against the investment income. The net investment income from intangible property shall be allocated to Georgia if the situs of the corporation is in Georgia or the intangible property was acquired as income from property held in Georgia, or as a result of business done in Georgia. The net investment income from tangible property located in Georgia shall be allocated to Georgia.

(2) Gains from the sale of tangible or intangible property not held, owned, or used in connection with the trade or business of the corporation nor for sale in the regular course of business shall be allocated to the State if the property sold is real or tangible personal property situated in the State, or intangible property having an actual situs or a business situs within

the State. Otherwise such gains shall be allocated outside the State.

(3) Net income of the above classes having been separately allocated and deducted, the remainder of the net business income shall be apportioned as follows: Where income is derived principally from the holding and/or sale of intangible property, having a taxable situs in this State, the tax should be imposed on the entire business income; if a portion of such intangible property has a taxable situs without the State, the portion of the income derived from the holding and/or sale of such property attributable to this State shall be taken to be such percentage as the gross receipts from such intangible property in this State for the taxable year bear to the total gross receipts from such sources: Provided, that the taxable situs of intangible property held or owned by any domestic corporation or by any foreign corporation whose principal place of business is in Georgia, shall be deemed to be in the State of Georgia, notwithstanding any domicile of any such corporation established elsewhere.

(4) Where income is derived from the manufacture, production, or sale of tangible personal property, the portion of the net income therefrom attributable to property owned or business done within this State shall be taken to be the portion arrived at by application of the following:

Three Factor Ratio.

(a) **Average inventory ratio.**—The ratio of the average of the monthly inventories of all products held in this State for sale, lease or other distribution or use in connection with the trade or business of the taxpayer during the taxable year to the average of the total monthly inventories of all products held every-

where for sale, lease or other distribution in connection with the trade or business of the taxpayer. The term "products" shall include goods, wares and merchandise of every character and kind, whether owned by the taxpayer or held on consignment or otherwise, but shall not include unrecovered or unextracted natural resources, raw materials, or goods in process of manufacture.

If the taxpayer shall fail to keep its records so as to disclose the information necessary to apply the foregoing ratio, the Commissioner shall determine the same from such information as may be available.

(b) **Salaries and wages ratio.**—The ratio of all salaries, wages, commissions, and other compensation paid or incurred by the taxpayer in this State for services performed in connection with the trade or business of the taxpayer during the taxable year to the total salaries, wages, commissions, and other compensation paid or incurred by the taxpayer in connection with its entire trade or business, wherever conducted, during the taxable year. For the purposes of this section, all salaries, wages, commissions and other compensation paid to residents of Georgia shall be deemed to have been paid or incurred in this State, irrespective of the place of actual payment.

(c) **Gross receipts ratio.**—The ratio of gross receipts from business done within this State to total gross receipts from business done everywhere. For the purposes of this section receipts shall be deemed to have been derived from business done within this State only if received from products shipped to customers in this State, or delivered within this State to customers, and in determining the gross receipts within Georgia, receipts from sales negotiated or effected through offices of the taxpayer outside the

State and delivered from storage in the State to customers outside the State shall be excluded.

(d) The average inventory ratio, the salaries and wages ratio, and the gross receipts ratio shall be separately determined and the three percentages averaged, and the net income of the corporation allocated and apportioned to Georgia according to such average.

(e) For the purposes of this section, the word "sale" shall include exchange, and the word "manufacture" shall include the extraction and recovery of natural resources and all processes of fabricating and curing.

(5) Where income is derived from business other than the manufacture, production or sale of tangible personal property, or from the holding or sale of intangible property, the net income shall be equitably apportioned within and without the State under rules and regulations of the State Revenue Commissioner, in the ratio that the business within the State is to the total business of the corporation.

(6) The net income of a domestic or foreign corporation which is a subsidiary of another corporation or closely affiliated therewith by stock ownership shall be determined by eliminating all payments to the parent corporation or affiliated corporation in excess of fair value, and by including fair compensation to such domestic business corporation for its commodities sold to or services performed for the parent corporation or affiliated corporation. For the purposes of determining such net income the Commissioner may equitably determine such net income by reasonable rules of apportionment of the combined income of the subsidiary, its parent and affiliates or any thereof.

3. **Section 92-2401 of the Code of Georgia of 1933**, the same being also Paragraph 43 of Section 1 of the General

Tax Act of 1935 (Ga. Laws 1935, pp. 11, 25); as amended (Ga. Laws 1951, pp. 157, 167; 1952, pp. 371, 372) and in effect during the years involved in this case:

> **Corporations, domestic and domesticated foreign.**—All corporations incorporated under the laws of Georgia, except those that are not organized for pecuniary gain or profit, and domesticated foreign corporations, in addition to all other taxes now required by them by law, are hereby required to pay each year an annual license or occupation tax as specified in the following scale: . . .

4. **Section 92-2403 of the Code of Georgia of 1933**, the same being also Paragraph 44 of Section 1 of the General Tax Act of 1935 (Ga. Laws 1935, pp. 11, 28) and in effect during the years involved in this case:

> **Foreign corporations.**—All corporations incorporated or organized under the laws of any other State, Territory, or Nation, doing business or owning property in this State, except those not operated for pecuniary gain or profit, in addition to all other taxes now required of them by law, are hereby required to pay each year an annual license or occupation tax for the privilege of carrying on their businesses within this State, as specified in the following scale: . . .